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Bear Stearns faces new round of hedge fund claims

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By Joseph A. Giannone

NEW YORK, Dec 5 (Reuters) - The first of a new round of investor claims was filed against Bear Stearns Cos. <BSC.N> on Wednesday for its role in managing two mortgage hedge funds that collapsed earlier this year, securities lawyers said.

The claims, which will be submitted to the Financial Industry Regulatory Authority (FINRA) for arbitration, represent more legal challenges for Bear Stearns, which recorded losses this summer.

The first of at least 11 new claims involves an unidentified Cayman Islands fund-of-hedge funds manager that lost \$1 million in the Bear Stearns High Grade Structured Credit Strategies Enhanced Leverage (Overseas) Fund.

FINRA keeps the names of arbitration parties confidential. Lawyers for the fund declined to identify their client. Bear Stearns spokesman Russell Sherman declined to comment, saying he had not seen the complaint.

Long considered one of the savviest bond traders on Wall Street, Bear Stearns suffered an embarrassing setback this summer as a rise in U.S. subprime mortgage defaults triggered a broader meltdown in mortgage-backed securities markets.



By the end of July, two funds managed by the bank -- Bear's High Grade Structured Credit Strategies Fund and the High Grade Structured Enhanced Leverage Fund -- had collapsed, wiping out about \$1.6 billion of investments.

Now a group of lawyers for 11 investors with combined \$62 million in losses says that Bear continued to sell shares of the funds this spring, when the subprime market was melting down.

According to the claim filed Wednesday, the unidentified fund-of-funds manager invested \$1 million in the Enhanced Leverage (Overseas) Fund in March 2007, when the subprime mortgage market was already showing some signs of strain.

By June there were market rumors that subprime investments in the fund had suffered steep declines. Bear on June 22 confirmed that margin calls were draining needed liquidity, and by the end of July, the two funds filed for bankruptcy.

"Officials at Bear Stearns engaged in a concerted effort to conceal the true state of affairs at both of these hedge funds for an extended period of time before they imploded," said lawyer Steve Caruso of Maddox, Hargett & Caruso in New York, one of four firms representing the fund-of-funds manager.

The lawyers claim Bear Stearns did not properly disclose "related-party" transactions between the funds and other Bear Stearns divisions, nor did it explain the risks of illiquid securities held by the portfolios.

As one of Wall Street's top underwriters of mortgage-backed securities, Bear Stearns knew or should have known these markets had become extremely unstable, said Ryan Bakhtiari of Aidikoff, Uhl & Bakhtiari.

"My gut feeling is these funds were used as a dumping ground by Bear Stearns," said Bakhtiari, whose Beverly Hills, California, firm is also representing the 11 claimants, along with Page Perry of Atlanta and David P. Meyer & Associates in Columbus, Ohio.

The claims come three weeks after Massachusetts Secretary of the Commonwealth William Galvin charged Bear Stearns with engaging in related-party trades without required approvals from independent directors.

Law firms Zamansky & Associates and Rich & Intelisano in August filed the first investor arbitration claim against the High Grade Credit Strategies Fund. Navigator Capital Partners, a limited partner in Structured Credit Strategies Fund, filed a civil lawsuit against Bear Stearns in Manhattan state court. (Editing by Steve Orlofsky)

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